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Highlights — 2004 Tax Law Changes

FS-2005-1, January 2005

Education Incentives

- The maximum **Tuition and Fees Deduction** is \$4,000 for those with Adjusted Gross Income (AGI) up to \$65,000 and \$2,000 for those with an AGI over \$65,000 but not over \$80,000. These AGI amounts are doubled for married persons filing jointly.
- Distributions from **Qualified Tuition Plans** (QTPs) maintained by private educational institutions are excludible up to the amount of qualified educational expenses. This tax break had been limited to State-sponsored QTPs.

Tax Credits

- The **Additional Child Tax Credit** is now refundable up to 15 percent of the amount by which earned income exceeds \$10,750. The rate had been 10 percent. Taxpayers with more than two qualifying children may be eligible for a larger credit. Nontaxable combat pay counts as earned income when figuring this credit.
- In computing the **Earned Income Tax Credit**, a taxpayer with nontaxable combat pay has the option of counting that pay as earned income, or omitting it. This has no effect on the amount of combat pay that is not taxed.

Retirement Plans / Individual Retirement Arrangements

- The **elective deferral limit** for 401(k), 403(b) and most 457 plan participants rose to \$13,000 (\$16,000 for 403(b) participants for whom the 15-year rule applies). For SIMPLE plans, the limit rose to \$9,000.
- The **catch-up contribution limit** for persons age 50 or older rose to \$3,000 for 401(k), 403(b) and 457 plans and to \$1,500 for SIMPLE plans.
- The \$10,000 phaseout range for **IRA deductions** for those covered by a pension plan begins at income of \$45,000 (\$65,000 if married filing jointly or a qualifying widow(er)). It still begins at zero for married persons filing separately.

Extension of Expiring Provisions

These provisions were left unchanged through 2005:

- Deduction for Educator Expenses
- Qualified Electric Vehicle Credit and Clean-fuel Vehicle Deduction
- Archer Medical Savings Accounts
- DC First-time Homebuyer Credit
- Allowance of nonrefundable personal credits against the alternative minimum tax

Miscellaneous Items

- When itemizing, taxpayers have the choice of deducting state and local income or **sales taxes**. An optional state sales tax table may be used in lieu of receipts for sales taxes paid. Sales taxes paid on a motor vehicle may be added to the table result, but only up to the amount paid at the general sales tax rate. Sales taxes on a boat, plane, home, or home building materials may be added if taxed at the general sales tax rate.
- For most **noncash charitable contributions** after June 3, 2004, taxpayers must satisfy these reporting requirements, based on the value of the deduction:
 - More than \$5,000 – obtain a qualified appraisal and attach Form 8283
 - More than \$500,000 (if art, \$20,000 or more) – attach a copy of the appraisal
- An “above-the-line” deduction is available for contributions to **Health Savings Accounts** made by April 15, 2005. The deduction is limited to the annual deductible on the qualifying high deductible health plan, but not more than \$2,600 (\$5,150, if family coverage). These limits are \$500 higher if the taxpayer is age 55 or older (\$500 each if both spouses are 55 or older). A person cannot contribute to an HSA starting the first month he or she is enrolled in Medicare.
- Taxpayers may not exclude any gain on the **sale of a principal residence** if they sold the property after Oct. 22, 2004, and had acquired it in a like-kind exchange during the five-year period ending on date of the sale.
- The **standard mileage rate** for business purposes rose to 37½ cents per mile. For medical or moving purposes, it rose to 14 cents per mile.
- Business taxpayers may take a **Section 179 expense** deduction for up to \$102,000 of qualifying equipment purchases, with this limit reduced by the amount that the total cost of section 179 property placed in service during the year exceeds \$410,000. The limit for certain sport utility and other vehicles that are not subject to the passenger auto limits and were placed in service after Oct. 22, 2004, is \$25,000.

IRS Publication 553, Highlights of 2004 Tax Changes, will have more details on the new provisions. It will be available in February 2005 through the IRS Web site, www.irs.gov, or by calling (toll-free) 1-800-TAX-FORM (1-800-829-3676).

Inflation Adjustments for 2004

The filing requirements, personal exemption, standard deduction and maximum Earned Income Tax Credit amounts are among the inflation-adjusted items.

- The 2004 gross income **filing requirements** are:

Single	\$ 7,950
Head of household	\$ 10,250
Married filing jointly	\$ 15,900
Married filing separately	\$ 3,100
Qualifying widow(er)	\$ 12,800

Different amounts apply if the taxpayer or spouse is age 65 or older, or if the taxpayer can be claimed as a dependent on someone else's return. There are also other specific situations that require the filing of a return, such as when the net earnings from self-employment are \$400 or more.

- The **personal exemption** amount for 2004 is \$3,100 — \$50 more than last year. Higher income taxpayers may have to reduce the personal exemption amount they claim if their adjusted gross income exceeds:

Single	\$ 142,700
Head of household	\$ 178,350
Married filing jointly or Qualifying widow(er) . . .	\$ 214,050
Married filing separately	\$ 107,025

These taxpayers use a worksheet in the tax package to figure their deduction for exemptions.

- The **standard deduction** amounts for 2004 are:

Single or Married Filing Separately	\$ 4,850
Head of household	\$ 7,150
Married filing jointly or Qualifying widow(er) . . .	\$ 9,700

Different amounts apply if the taxpayer or spouse is blind or is age 65 or older, or if the taxpayer can be claimed as a dependent on someone else's return.

- The **Earned Income Tax Credit** amounts for 2004 are:

<u>Qualifying child</u>	<u>Income Under*</u>	<u>Max. Credit</u>	<u>Income for Max. Credit</u>
One	\$ 30,338	\$ 2,604	\$ 7,650 — 14,049*
Two or more . .	\$ 34,458	\$ 4,300	\$10,750 — 14,049*
None	\$ 11,490	\$ 390	\$ 5,100 — 6,399*

(*These amounts are \$1,000 higher for married persons filing joint returns.)

The maximum amount of investment income a person may have and still be eligible for the Earned Income Tax Credit increased to \$2,650.